



COMPTROLLER GENERAL OF THE UNITED STATES
WASHINGTON 25

B-55649

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The Honorable,

The Secretary of State.

My dear Mr. Secretary:

I have your letter of January 29, 1946, as follows:

"Contract of lease no. 89 fa-56 dated September 26, 1935 covers five buildings with servants' quarters and garages located at the junction of Shanghai and Ningpo Roads in Nanking, China. The lease was made between the Sin Hwa Trust and Savings Bank, Limited, as lessor, and the Secretary of State of the United States of America, acting by Willys E. Peck, Counselor of the American Embassy at Nanking, as lessee. In pursuance of said contract, the lessor constructed these buildings for use as office and living quarters for the American Embassy at Nanking. The lease stipulates a rental of 3000 yuan dollars per month to be paid in advance commencing on the date the premises are accepted by the lessee as ready for occupancy. The premises were accepted for occupancy on August 28, 1936 as evidenced by a certificate of commencement of the lease signed by the lessee and the lessor. The lease expires on August 28, 1947. Both the lease in question and the certificate of commencement of lease were transmitted to the Audit Division of the General Accounting Office respectively under cover of this Department's letters of November 12, 1935 and March 5, 1937.

"Reports received through the Swiss, who were representing American interests, indicate that by August, 1943, the Japanese had occupied these premises.

"On September 18, 1945, a contingent of the American Embassy at Chungking, China, arrived at Nanking for the purpose of making preparations incident to the removal of the seat of the Chinese Government from Chungking to Nanking where it is contemplated the American Embassy will be located in the not too distant future.

"Because of the Japanese occupation and with the passage of time, these buildings have undergone deterioration. Under the terms of the lease, the lessor is charged with making repairs. Conditions have drastically changed since the contract was entered into, the most crucial change being extreme inflation in China. Inflation has gone to such an extent that the lessor is now receiving, in terms of United States currency, between two and three dollars per month.

Statements from American Foreign Service representatives make manifest that the lessor finds himself in financial straits. This Department has instructed its representatives in China that under the lease the landlord is obligated to maintain the premises in good repair and tenable condition, except for damage or negligence of the lessee, his agents, or employees, and it has also been pointed out that, under Article 11 of the lease, the Government can take measures to establish conditions contemplated by the contract in the event that the lessor fails to fulfill any of its conditions, provided the matter is brought to the landlord's attention on more than one occasion and provided the landlord has refused to take the desired action or has delayed beyond a reasonable time in acting on the tenant's request. This Department's representatives were instructed to notify the lessor accordingly in writing, under the provision of Article 11. In as much as the rent under the lease brings the landlord only two or three dollars, American currency, per month on rather extensive properties, it will readily be perceived that this Department cannot very well bring about the terms contemplated by the lease by taking the initiative in making repairs and deducting such costs from the rent payments.

"The Department's representative at Nanking has recommended, in compliance with the lessor's request, that the contract be revised so as to provide for a monthly payment of one thousand United States dollars, effective from September 18, 1945, the date on which these premises were reoccupied. The \$1000 figure is calculated to place the lessor in his original position.

"This Department is aware of decisions of the Comptroller General which hold that a landlord is bound by the terms of his lease notwithstanding changes in circumstances. On the basis of those decisions, it is this Department's understanding that 'Where one agrees to do, for a fixed sum, a thing possible to be performed, he will not be excused or become entitled to additional compensation, because unforeseen difficulties are encountered.' (Comp. Gen. Decision B-49226, June 11, 1945). Decisions of this nature are supported by American law. It would appear, however, that a contract such as this, made in China, having been and to be performed in China, would be subject to construal in the light of Chinese law. In this connection, this Department has been advised that, under Chinese law, when a lease is for a definite period the Chinese Courts have discretionary power to grant equitable relief under Article 246 of the Civil Code which provides:

"A contract for an impossible prestation is void. However, if the impossibility can be removed and if the parties, at the time when the contract was concluded, intended to have it performed after the removal of the impossibility, the contract is valid.' (Translated by Ching-lin Hsia et al.)

"It is understood that in construing this Article a Chinese Court would probably consider three important factors: First, the Confucian

Doctrine of Tao I which may be translated as 'justice and righteousness'. This doctrine is the foundation of what may be loosely designated as the Chinese Law of Equity. In applying this doctrine the judges possess broad discretionary powers and are only required to render their judgments in accordance with 'justice and righteousness' and the dictates of their consciences. This system of equity is one which is compatible with Chinese psychology. The second factor is custom, the applicability of which is specified in Articles 1 and 2 of the Civil Code as follows:

"Article 1 — 'In civil matters if there is no provision of law applicable to a case, the case shall be decided according to custom. If there is no custom, the case shall be decided in accordance with the general principles of law.'

"Article 2 — 'A custom is applicable in civil matters only when it is not contrary to public order or good morals.'

"The third factor is the ability of the parties to pay and/or to perform.

"This Department has been advised that all of the essential elements seem to be present in this case. Namely, that it would be just and righteous according to Chinese equity to re-adjust the rental; that Chinese custom requires that rents be re-adjusted when there is a sharp rise or decline in the value of the currency; and that the United States is able to pay an adjusted rental and will be unwholly enriched if it continues to pay the original rental of 3,000 Yuan dollars per month; while on the other hand the landlord is financially unable to maintain the premises, as he is required to do by the lease and Chinese law, unless he receives an adequate rental.

"After taking all the facts and circumstances into consideration it would seem that the landlord could prove a strong prima facie case in a Chinese Court, if it had jurisdiction, entitling him to equitable relief.

"It should be pointed out that Chinese law does not strictly adhere to the doctrine of stare decisis and that 'equity' jurisprudence in China is more elastic and less fixed than American equity jurisprudence. Citations of recent Chinese decisions therefore would not be conclusive even if they were now at hand.

"It is further understood that a Chinese Court, guided by the stated considerations, would likely be disposed to rule that a compromise figure be established which would result in having the lessee assume part of the disadvantage now being solely borne by the lessor.

"In addition to the purely legal aspects of the question which are discussed above, the question of the national interest of the United States should be given serious consideration as one of the determining factors. As stated in a telegram from the Embassy at Chungking, to insist, on a basis of legal rights, upon retaining possession of this

valuable property at such a ridiculously low rental in the face of China's present drastic inflation would greatly injure the reputation of the United States in China for equity, justice and sense of fair play. The landlord, moreover, has been very accommodating to us in the past and it is believed that his actions in pressing for a revision of the lease agreement are dictated solely by necessity and consideration of equity. A further consideration is the fact that the same landlord is at present renting us one other building on a highly desirable site which it is necessary that we retain. If, however, the landlord is not granted relief with respect to the lease agreement on the original Embassy property, it is virtually certain that he will further embarrass this Government by disposing of the additional building by sale to another government.

"It is eminently desirable, therefore, that a decision be made enabling this Department to enter into a supplemental agreement by which the lessee undertakes to increase the monthly rental to not to exceed \$500, United States currency, which would be approximately equivalent to fifty per cent of the original rent, on the understanding that this increase shall become effective on July 1, 1946, at which time it is contemplated that the American Embassy at Nanking will be in full operation, and to pay rent for the 1947 fiscal year in one installment on July 1, 1946 and on July 1, 1947 for the period July 1 to August 28, 1947. This would assure this Government of the proper maintenance of the premises by the lessor and would lessen criticism of this Government for harsh insistence on the letter of the contract."

It is understood that, at the rate of exchange prevailing as of the effective date of the instant lease, or August 28, 1936, the stipulated rental rate in terms of United States currency was approximately \$1,120 per month. Hence, as indicated in your letter, a monthly rental rate of \$500 in United States currency would be approximately 50 percent of the original rental rate. While the lease provides for cancellation by the Government prior to the expiration of the original term or the renewal thereof as set forth in paragraphs 5 and 6 of said lease, there are no corresponding options in favor of the lessor. Moreover, while, by its terms, the lease expires after eleven years, or on August 28, 1947, paragraph 6 provides that occupancy may be continued for an additional period of five years subject to terms mutually agreed upon by the parties at the termination of ten years of occupancy. Consequently, amendment of the lease so as

to insure restoration of the premises would appear to be in the Government's interest in order that occupancy may be continued for five years beyond August 28, 1947, if such be deemed necessary and desirable by your Department.

Accordingly, and since, as indicated in your letter the rights and obligations of the parties under the lease probably would be determined under the law of China and, as set forth further therein, the courts of China probably would relieve the lessor from its obligation to restore the premises under the facts herein present, I have to advise that, if your Department should determine to amend the original lease by supplemental agreement as proposed in the concluding paragraph of your letter, no objection thereto will be interposed by this office. It is to be understood, of course, that the appropriations available for the payment of rental will be sufficient for the increased rental under the proposed supplemental agreement. See Section 3679, Revised Statutes, as amended.

Respectfully,

(Signed) Lindsey C. Warren

Comptroller General
of the United States.